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BEFORE THE

Federal Communications Commission

WASHINGTON, D.C.

In the Matter of the Application of	)	
	)	CC Docket No. 94-1
Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation	)	

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COMMENTS OF THE NATIONAL CABLE TELEVISION ASSOCIATION, INC. IN THE THIRD FURTHER NOTICE OF PROPOSED RULEMAKING

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ECONOMIC AND TECHNOLOGY
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October 27, 1995

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The National Cable Television Association, Inc. ("NCTA") hereby files its Comments in the Third Notice of Proposed Rulemaking in the above-referenced proceeding.[1]

INTRODUCTION

In the Second Report and Order, the Commission took a significant step toward facilitating the identification of cross-subsidy by LECs that offer video dialtone ("VDT"). The creation of a separate VDT price cap basket that is excluded from the sharing process will make it more difficult for LECs to disguise the costs of video services as investments in telephone services.

In the Third NPRM, the Commission has now raised two additional issues regarding the VDT price cap basket, both of which it appears to view solely as aspects of the implementation

[1] See Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation, Second Report and Order and Third Further Notice of Proposed Rulemaking, CC Docket No. 94-1 (released September 21, 1995) ("Third NPRM").

of its VDT price cap basket decision. The first of these issues, namely the proposed de minimis threshold below which VDT investment will not be excluded from the sharing process,[2] is indeed such an implementation issue. As explained below, NCTA opposes the adoption of any de minimis threshold. If the Commission decides to impose such a mechanism, however, it should set it at the amount of dedicated and shared interstate VDT investment required to reduce a LEC's rate of return by 10 basis points.

The second issue concerns "the method or factor to be used in Part 69 for allocating video dialtone costs to the video dialtone basket."[3] Unlike the de minimis threshold, this question implicates far more than the implementation of the VDT basket decision. As NCTA has often stressed, the only way for the Commission to determine the proper method of allocating VDT is to make a policy decision as to who should bear the cost of the VDT upgrade. That choice constitutes the most important decision regulators will make in the VDT context. The Commission must ensure that it is understood as such, and not as simply a subsidiary aspect of the implementation of a separate VDT price cap basket. Moreover, the Commission must ensure that Parts 61 and 69 as well as all other processes are implemented in a manner consistent with that choice.

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2 See id. at ¶¶ 39-40.

3 Id. at ¶ 41.

DISCUSSION

I. The Allocation Of VDT Costs And The Establishment Of VDT Tariffs Should Be Based On Clear And Explicit Policy Goals.

In the instant NPRM, the Commission appears to have finally begun to consider the manner in which the costs of VDT should be allocated among telephony and video services. While NCTA is encouraged by the Commission's willingness to confront this critical issue, it is concerned that the FCC is still unwilling to recognize either the importance of this issue or the proper way in which to approach it.

A. The Commission Still Fails To Properly Acknowledge the Significance of the Allocations Process.

NCTA is concerned, as it has been throughout the VDT proceedings, that the Commission address the allocation issue as part of a larger *policy* choice as to who should pay for the VDT upgrade. As mentioned, the Commission invited parties to comment on "the method or factor to be used in Part 69 for allocating video dialtone costs to the video dialtone basket."[4] But while this decision should not be the result of regulation by default, it appears that this may happen. After continuously stressing the importance of this issue, NCTA and other interested parties have seen allocations first addressed in a single, rather confusing paragraph at the end of a notice on a separate VDT price cap.

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[4] Id.

The allocation issue is the most important policy decision the FCC will make in this regulatory proceeding. A separate price cap basket is simply a way of enforcing that decision. Moreover, as NCTA has consistently maintained, choosing an accounting construct, such as the new services cost allocation methodology and the fixed cost allocation factor mentioned in the Third NPRM, is not the same as making an open choice on the allocation issue. Until the FCC makes the allocation choice, NCTA cannot recommend the appropriate accounting approach.

In sum, the Commission must not permit the seminal allocation issue to become subsidiary to the VDT price cap basket proceeding, and it should not avoid the issue by characterizing it as simply a matter of choosing the proper accounting mechanism. The Commission should devote the necessary attention and resources to this issue. Moreover, it should characterize its decision as a policy choice of the responsible administrative agency as to the amount of VDT investment monopoly telephone ratepayers will be required to bear.[5]

B. The Commission Must Ensure That It Employs A Consistent Approach To Both Allocations And Tariffs.

As NCTA and other parties to this proceeding have explained before, VDT service will share substantial costs with differently regulated services, and can only be effectively supervised by

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[5] The Commission should also, as several parties including NCTA have argued, create a separate Part 69 category for VDT. This is a necessary part of any allocation of costs to VDT.

addressing each step in the regulatory process in the proper order. In broad terms, this means that the total costs, dedicated and shared, should first be captured in Part 32 accounts. The Commission should then make an explicit policy decision as to the manner in which the shared costs and overhead costs are to be allocated. Finally, the costs allocated to video transmission should become the basis for tariffed prices.

In VDT, the Commission has reversed the proper order of allocations and the tariff review. In RAO Letter 25, it properly attempted to capture the shared and dedicated costs of VDT.[6] However, rather than proceeding with an allocation decision, as it should have, the Commission went on to choose a scheme, the new services test, for evaluating VDT rates in the tariff process.

As the Commission acknowledged in the Reconsideration Order,[7] the new services test does not require fully distributed costing.[8] The result is that telcos are permitted to charge lower prices for VDT than another tariff test might permit. NCTA maintains that the new services test is inappropriate in both the *pricing* context and the *allocations* context. The correct

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6 See RAO Letter 25, DA 95-703 (released April 3, 1995).

7 See Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54-63.58 and Amendments of Parts 32, 36, 61, 64, and 69 of the Commission's Rules , Memorandum Opinion and Order on Reconsideration and Third Further Notice of Proposed Rulemaking, 10 F.C.C.R. 244 (1994).

8 See id. at 345, ¶ 218.

approach to allocations is an approach that takes account of an appropriate share of the common costs.

In the instant Notice, the Commission has in fact raised the possibility that it will not adopt the new services test as the allocations standard.[9] If the Commission decides to adopt a methodology for allocations other than the new services test, then the pricing and allocations approaches will obviously be different. The result may be that VDT rates that appear to meet the requirements of the new services tariff test will fail to meet the VDT allocations requirements.

The critical point is that the allocations and tariff approaches must be made consistent. Moreover, the Commission's allocation decision should dictate the resolution of any differences between the pricing and allocation tests. As a result, the Commission's decision on allocations may well require it to reconsider its adoption of the new services test for VDT tariffs.

II. The Commission Should Not Establish A De Minimis Threshold For VDT Investment Included In Sharing.

The Commission has proposed to establish a de minimis threshold below which LEC investment in VDT will not be excluded from the sharing process.[10] NCTA opposes this position because

[9] See Third NPRM at ¶ 41.

[10] Although the Commission adopted this position as part of the Order, it did so without first soliciting comment from interested parties on the subject. An agency may not adopt rules without first permitting interested parties the opportunity to (continued...)

the administrative burden associated with excluding all VDT investment from sharing is in fact extremely small. Indeed, RAO Letter 25 already requires LECs to track the costs of VDT. Once the Commission makes the required decisions concerning the allocation of shared and common costs, flowing the cost information through to the reports needed to implement sharing is simply a matter of implementing minor modifications to the necessary forms.

Moreover, a de minimis threshold would add administrative burdens. Any telco that exceeds the threshold would presumably have to remove all of the costs previously included in the sharing process. It is difficult to see why this would not create an even greater administrative burden than simply removing all VDT investment from the sharing process.

If, however, the Commission decides to adopt a de minimis threshold, it must ensure that it does not permit LECs to cross-subsidize significant amounts of VDT investment. In short, the Commission should set the de minimis level at the amount of dedicated *and* shared VDT investments[11] required to reduce a LEC's rate of return by a small amount. We recommend 10 basis points.

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[10](...continued)
submit comments. See 5 U.S.C. § 553. Accordingly, NCTA has submitted comments on *whether* the Commission should adopt a de minimis standard.

[11] As stated, these costs are captured in the Commission's RAO Letter 25.

Setting the threshold higher than 10 basis points would permit LECs with larger amounts of costs attributed to interstate regulated services to concentrate significant investments in selected VDT markets before the sharing exclusion is triggered. For example, NCTA estimates that Bell Atlantic's total plant in service can grow by $138 million dollars before its rate of return for interstate regulated services would fall from 11.25% to 11%. This amount exceeds the total first year dedicated investment for five of the systems once proposed, but since withdrawn, by Bell Atlantic. These five systems would have been capable of potentially serving almost one million subscribers.[12] A large carrier like Bell Atlantic could therefore make a very substantial investment in broadband markets before meeting a de minimis standard. This level would be too high.

Furthermore, counting only dedicated costs, as the Commission suggests,[13] would arbitrarily benefit LECs that have constructed systems with integrated rather than stand-alone facilities. It might also create the incentive to build integrated systems, regardless of whether such designs are the most efficient.

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[12] In its December 16, 1994 letter response to a Common Carrier Bureau request for information, Bell Atlantic indicated that its projected direct investment in Baltimore, Northern New Jersey, Tidewater, Philadelphia and Pittsburgh would total $124 million dollars in the first year. See Letter from Marie T. Breslin to William Caton, transmitting Bell Atlantic Response to Inquiries, Exhibit 3, W-P-C-6966 (December 16, 1995).

[13] See Third NPRM at ¶ 41.

Setting the threshold at the amount of dedicated and shared interstate VDT investment required to reduce a LEC's rate of return by 10 basis points could mitigate these potentially damaging effects.

CONCLUSION

NCTA respectfully requests the Commission to base the allocation of VDT investment on an explicit policy choice as to whom should bear the costs of the VDT upgrade. NCTA also requests that the Commission abstain from adopting a de minimis threshold for VDT investment that is included from the sharing mechanism.

Respectfully submitted,

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